



March 31, 2020

Attention to: Ms. Ann E. Misback, Secretary, **Board of Governors of the Federal Reserve System (FED)**  
Ms. Vanessa A. Countryman, Secretary, **Securities and Exchange Commission (SEC)**  
Mr. Christopher Kirkpatrick, Secretary, **Commodity Futures Trading Commission (CFTC)**  
Mr. Robert E. Feldman, Executive Secretary, **Federal Deposit Insurance Corporation (FDIC)**  
Chief Counsel's Office, **Office of the Comptroller of the Currency (OCC)**

Email: [regs.comments@federalreserve.gov](mailto:regs.comments@federalreserve.gov); [rule-comments@sec.gov](mailto:rule-comments@sec.gov); [regs.comments@occ.treas.gov](mailto:regs.comments@occ.treas.gov); [comments@FDIC.gov](mailto:comments@FDIC.gov)

Subject: **Proposed Revisions to Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds**

Agency	Docket No./ File No.	RIN
DEPARTMENT OF TREASURY - OCC	OCC-2020-0002	1557-AE67
FED	R-1694	7100-AF70
FDIC		3064-AF17
SEC	S7-02-20	3235-AM70
CFTC		3038-AE93

On behalf of **Data Boiler Technologies**, I am pleased to provide the FED, SEC, CFTC, FDIC, and OCC (collectively, the "Agencies") with comments and thanks for acknowledging our prior comments 9 times in the preamble of the agencies' proposal to revise section 13 of the Bank Holding Company Act (a.k.a. the Volcker Rule).<sup>1</sup> This proposal is considered in midst of a global financial turmoil that triggered by the novelty Coronavirus (CoVID-19) situation. Indeed, this is exactly the moment I long advocated for the need of and referred to as "Stress RENTD". It is time for banks to pour liquidity to markets and temporarily lifting related regulatory restrictions on their ability to scoop up troubled assets to restore financial stability.

As I have said in my comment to OCC in 2017<sup>2</sup> and additional comments to all 5 agencies in 2018<sup>3</sup>, the Volcker's covered fund requirements are the Rule's heaviest burden as compared to proprietary trading. My 2018 estimate of covered fund compliance cost for the top 46 banks are between \$152 million to \$690 million, excluding the \$3.63 billion expected loss from divesting impermissible toxic assets (5.5% x \$66 billion) in their portfolio per the OCC's original analysis of 12 CFR Part 44<sup>4</sup>. It may be a crowded market when everyone rushes to off-load these assets as it draws closer to the 2022 deadline. The sooner banks can get rid of these toxic positions, the less capital surcharge for them. However, the current financial turmoil is definitely not the right time to ask banks for a stable runoff of these assets, or it is practically impossible during this crunch time.

That being said, we are in support of temporary relief of compliance burden and limited revisions to the Rule's covered fund provisions. However and please make no mistake about our strong opposition to the many changes to the Rule's proprietary trading provisions – RENTD in particular<sup>5</sup>. As we have seen how other countries swept their troubled assets under the rug<sup>6</sup>, their banks are trading at substantially lower multiple than our banks in the

<sup>1</sup> <https://www.sec.gov/rules/proposed/2020/bhca-8.pdf>

<sup>2</sup> <https://www.regulations.gov/document?D=OCC-2017-0014-0013>

<sup>3</sup> [https://www.databoiler.com/index\\_htm\\_files/DataBoiler%202018Comments%20VolckerRevision.pdf](https://www.databoiler.com/index_htm_files/DataBoiler%202018Comments%20VolckerRevision.pdf)

<sup>4</sup> [https://www.databoiler.com/index\\_htm\\_files/OCC%20Analysis%20of%2012%20CFR%20Part%2044.pdf](https://www.databoiler.com/index_htm_files/OCC%20Analysis%20of%2012%20CFR%20Part%2044.pdf)

<sup>5</sup> [https://www.databoiler.com/index\\_htm\\_files/DBTPublicStatementVolckerRevision.pdf](https://www.databoiler.com/index_htm_files/DBTPublicStatementVolckerRevision.pdf)

<sup>6</sup> [http://www.huffingtonpost.com/entry/china-financial-crisis\\_us\\_587cfe4fe4b0b3c7a7b23394](http://www.huffingtonpost.com/entry/china-financial-crisis_us_587cfe4fe4b0b3c7a7b23394)



US. If the agencies choose to permanently water down prudential rules and banks' compliance standards, allow me to remind everyone that these short-term gratifications would come at an expense detriment to our long-term soundness and prominent leadership position around the World's banking industry.

The agencies, and the FED in particular, should take a more restrain and long-term view to our Country's financial policy and seek ways to ensure that the cumulative effects of such deferred treatment of toxic assets would not inadvertently lead to other problems that may cascade or lead to uncontrollable or difficult to control consequences, or prevents the abuse of the temporary tolerance process to bypass prudent controls. Also, we have reservations toward some of the backward thinking by former FDIC Vice-Chair Hoenig<sup>7</sup>. To quote him, he calls for a "return the safety net to its original purpose—that of protecting the payments system and the depositor." Banks are not merely payment processors and deposit takers in the 21st century! It is better for banks to play the market maker role in serving the economy, than pushing investment banking functions out to the shadow banking system and High Frequency Trading firms<sup>8</sup>. The FDIC should not simply pass the buck to let other agencies deal with modern days' financial engineering problems. His suggestion to partition commercial and investment banking activities by creating separate legal entities only benefits law firms.

In our opinion, there exist an opportunity to streamline the Rule's covered fund provision by rewritten it to become the 21st Century Glass-Steagall Act<sup>9</sup>. To ensure shifted risks would not come back to haunt banks, the industry as a whole may look into the asset gathering and fund distribution processes (e.g. monitor the banking entity's investments in, and transactions with, any covered funds), and use behavioral science to ensure "exit only, no re-entry" – like "letting go"<sup>10</sup> of bad habits/toxic assets. We will be glad to discuss further specifics with the regulators, industry groups, and banks, and/or testify in front of Congress upon request.

We hope the above high level comments and the detailed responds to specific questions below will be helpful to the agencies and benefiting the broader industry and economy. Feel free to contact us with any questions. Thank you and we look forward to engage in any opportunities where our expertise might be required. Blessing and stay well amid the Coronavirus situation.

Sincerely,

[Kelvin To](#)

*MSc Banking, MGMT, BSc*

**Founder and President**

**Data Boiler Technologies, LLC**

This letter is also available at:

[https://www.DataBoiler.com/index.htm\\_files/DataBoiler%202020Comments%20VolckerRevision.pdf](https://www.DataBoiler.com/index.htm_files/DataBoiler%202020Comments%20VolckerRevision.pdf)

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<sup>7</sup> <https://www.fdic.gov/news/news/speeches/spmar1317.html>

<sup>8</sup> <https://www.linkedin.com/pulse/too-many-stakes-volcker-kelvin-to/>

<sup>9</sup> <https://www.linkedin.com/pulse/volcker-rule-mocked-vs-revisions-kelvin-to/>

<sup>10</sup> <https://www.bakadesuyo.com/2016/04/bad-habits/>



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## A.) Qualifying Foreign Excluded Funds

With due respect to the IIB's (Institute of International Bankers) arguments<sup>11</sup> about "permitting the U.S. operations of foreign banking organizations to engage in proprietary trading in the sovereign obligations of their home countries under Section \_\_.6(b) of the 2013 Rule is consistent with the authority in Section 13(d)(1)(J)", yet it is not without conditions.

I acknowledged that some foreign banks might want to enable foreign sovereign governments to conduct monetary policy or finance their operations and keep the money market operations of foreign central banks functioning by scooping up foreign sovereign obligations during this time of pandemic crisis and possible global recession. Those are good intents to rescue the global financial markets from possible melt down. However, the agencies do not provide comprehensive guideline on how the proposed relief would be limited to the asset management activities of foreign funds, and for example what criteria the agencies plan on using when applying their discretion to determine that the activity in question would "promote and protect the safety and soundness of the banking entity and the financial stability of the United States" under section 13(d)(1)(J) of the BHC Act. If it is going to be 100 out of 100 times that the agencies are granting relief, that is in effect a "carve out".

The agencies' proposal is against President Trump's "America First" Principle<sup>8</sup> and it may have inadvertent effect to direct fund flow away from US Treasury, US agencies' bonds, or other US based securities. Also, what "If" G-SIBs consider this foreign exclusion "carve out" as an escape from compliance burden, and decide to change their domicile away from the US? Although this is a remote scenario, but regulatory authorities should not undermine a possibility for fundamental shift in banking market structure around the Globe and related implication to the shadow banking sector.

Thankfully, there are alternative ways, such as SOTUS exemption and the FED's no action relief<sup>12</sup>, under the existing Rule to grant appropriate reliefs for foreign banks. "If" additional relief is to be considered, I think a temporary relief (Stress RENTD) based on prevailing market turmoil is more suitable than a permanent relaxation of the Rule. Under "Stress RENTD", banks around the World would be on equal footing about proprietary trading, rather than regional differences in compliance burden.

As a reminder, the current Rule does not preclude banks to be debt holders of foreign excluded funds. Banks don't have to be equity owner. Debts indeed give banks a priority claim over assets of foreign excluded funds in case of default, which is safer than banks being equity owner. After all, given the current market volatility condition, it is hard to ensure any risks associated with the activities conducted by the foreign funds would remain outside the US. Especially, the US has yet to implement a robust

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<sup>11</sup> <https://www.fdic.gov/regulations/laws/federal/2018/2018-proposed-revisions-to-prohibitions-proprietary-trading-3064-ae67-c-070.pdf>

<sup>12</sup> <https://www.federalreserve.gov/newsevents/pressreleases/files/bcreg20170721a1.pdf>





mechanism to ensure “exit only, no re-entry” or use behavioral science to “let go”<sup>10</sup> of toxic assets. Therefore, temporary relief under “Stress RENTD” is a better approach than the agencies’ proposal.

**Question 1.**

Should the agencies make any other amendments to §§ \_\_.6 and \_\_.13 or include any additional parameters on the proposed exemption? Why or why not?

NO. Temporary relief under “Stress RENTD” is a better approach. Please see earlier paragraphs in this section for explanations.

**Question 2.**

Would the proposed amendments to §§ \_\_.6 and \_\_.13 address the concerns raised regarding unintended consequences and extraterritorial impact? Why or why not? If the amendments would not address these concerns, what other amendments should be made?

The agencies proposal indeed would create other unintended consequences detrimental to competitiveness of banks in the US. Please see earlier paragraphs in this section for explanations.

**Question 3.**

Is the proposed approach to addressing foreign excluded funds effective? Why or why not? If not, what alternative approach would better address these types of entities?

Easing foreign banks’ concerns at the expense of putting US economy and US banks at a disadvantage is not recommended. Please see earlier paragraphs in this section for explanations.

**Question 4.**

Would the use of the term “covered fund” in § \_\_.13(b)(1) or in proposed § \_\_.13(d)(2), together with the definition of “covered fund” in § \_\_.10(b)(1), create any unintended consequences for foreign banking entities seeking to rely on the exemption for activities permitted by section 13(d)(1)(I) of the BHC Act? Why or why not? If so, what other alternatives should be considered to make the exemption for activities permitted by section 13(d)(1)(I) of the BHC Act clear or more workable?

Regardless of how the agencies are trying to articulate with the “covered fund” terminology, the said relief is indeed a “carve-out” as long as whatever foreign funds fit the foreign banks’ asset management category. How the agencies would use their discretion under section 13(d)(1)(J) of the BHC Act to restrain possible misuse of this “carve out” is a big unknown. Again, I suggest using “Stress RENTD” as a temporary relief instead of the agencies’ proposal.

**Question 5.**

What impacts would the proposed amendments to §§ \_\_.6 and \_\_.13 have on the safety and soundness of banking entities, and on the financial stability of the United States? Would the activities permitted under the proposed amendments to §§ \_\_.6 and \_\_.13 of the regulations promote and protect safety and soundness and U.S. financial stability? Please explain.





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Inadvertent effect to direct fund flow away from US Treasury, US agencies' bonds, or other US based securities (e.g. Canadian government bonds may offer better yield). The market is highly volatile now, and the change in Rule may trigger unforeseen consequences that shaking US leadership position in global financial market. Please see earlier paragraphs in this section for elaborated thoughts.



## **B.) Modifications to Existing Covered Fund Exclusions**

### **1. Foreign Public Funds**

The agencies' proposal about foreign public fund is less than ideal for maximum control but it is acceptable from practical implementation standpoint. Foreign public funds would remain "limited to funds that are authorized to be sold to retail investors, but it would no longer require the fund to be authorized to be sold to retail investors in the jurisdiction where it is organized" as the agencies have stated.

The new requirements make sense that the distribution is subject to "substantive disclosure and retail investor protection laws or regulations, to help ensure that funds qualifying for this exclusion are sufficiently similar to U.S. registered investment companies" and only applicable when "the banking entity acts as the investment manager, investment adviser, commodity trading advisor, commodity pool operator, or sponsor" because tracking the sale of ownership interests to employees and their immediate family members is extremely difficult if not impossible. I see these new requirements as reasonable "trade-offs" to eliminate the limitation on selling ownership interests of the issuer to employees of the sponsoring banking entity or the issuer and eliminate the requirement that it be sold "predominantly" through one or more public offerings.

#### **Question 6.**

Are foreign funds that satisfy the proposed conditions in the foreign public fund exclusion sufficiently similar to U.S. registered investment companies such that it is appropriate to exclude these funds from the covered fund definition? Why or why not? If these foreign funds are not sufficiently similar to U.S. registered investment companies, how should the agencies modify the exclusion's conditions to permit only funds that are sufficiently similar to U.S. registered investment companies to rely on it? Are there foreign funds that cannot satisfy the exclusion's proposed conditions but that are nonetheless sufficiently similar to U.S. registered investment companies such that it would be appropriate to exclude those foreign funds 31 from the covered fund definition? If so, how should the agencies modify the exclusion's conditions to permit those funds to rely on it?

Not 100% but acceptable from a practical standpoint to balance between compliance costs and benefits. The said new disclosure requirement in the agencies proposal should offer enough transparency.

#### **Question 7.**

How effectively does the proposed replacement of the home jurisdiction requirement and the requirement that ownership interests be sold predominantly through public offerings with a requirement that the fund is authorized to offer and sell ownership interests, and such interests are offered and sold, through one or more public offerings address the concerns discussed above related to the compliance with these requirements? If such concerns are not addressed, how should the agencies further modify these requirements?



Yes, good enough. Thanks!

#### Question 8.

Is the additional condition added to the “public offering” definition requiring the distribution be subject to substantive disclosure and retail investor protection laws or regulations sufficiently clear and effective? If not, how should the agencies modify or clarify this requirement? Should the agencies further specify features of “substantive disclosure and retail investor protection laws or regulations?” Would it be clearer if the agencies identified particular types of laws or regulations that would meet this condition (e.g., requirements for periodic filings with, and periodic examinations by, the appropriate regulatory authority; requirements for periodic reports to be distributed to retail investors; or a prohibition against fraud)?

There should be some flexibility in terms of disclosure, or else it would only benefit those big law/consulting firms. After all, “no fish would be able to survive if the water is overly clear” and I believe one person’s trash could be another’s treasures.

#### Question 9.

In what ways, if any, is it difficult for a banking entity to determine whether a fund satisfies the implementing regulations’ condition of the “public offering” definition requiring that the distribution comply with all applicable requirements in the jurisdiction in which the distribution is made? Should the agencies eliminate this requirement with respect to funds for which the banking entity does not serve as the investment manager, investment adviser, commodity trading advisor, commodity pool operator, or sponsor, as proposed, or should this requirement be otherwise modified? Would eliminating or modifying this requirement create an opportunity for evasion of the requirements of section 13? If so, how should the agencies address this concern?

No, this requirement should not be eliminated. This is one of the essential criteria that we accept related “trade-offs”. Please see earlier paragraphs in this section for explanations.

#### Question 10.

As discussed above, the agencies propose to modify the additional conditions on U.S. banking entity-sponsored foreign funds, which are intended in part to limit the possibility for evasion of section 13. In what ways, if any, would the proposed modifications, including the elimination of the limitations on certain employees owning interests in the fund, create an opportunity for evasion? How should the agencies modify these additional requirements to limit the possibility for evasion? Is the limitation on directors and senior executive officers owning interests in the fund necessary or appropriate to prevent evasion of section 13? Why or why not? Should the agencies eliminate or modify this limitation? How difficult is it for banking entities to monitor and track this limitation? Commenters should address whether banking entities already track this information.

Please refer to our respond in the [Error! Reference source not found.](#) section.



## Question 11.

Is the proposed requirement that the fund's ownership interests are sold predominantly to persons other than the sponsoring banking entity or the issuer (or affiliates of the sponsoring banking entity or issuer), and directors and senior executive officers of such entities, necessary to prevent evasion of the requirements of section 13? If the requirement is not necessary to prevent evasion, how should the agencies eliminate or further modify this requirement? Should the agencies consider this condition satisfied if 75 percent (or some other percentage) of the ownership interests are sold to persons other than the sponsoring banking entity, the issuer (or affiliates of the sponsoring banking entity or issuer), and directors and senior executive officers of such entities? Why or why not?

The agencies should preserve the FAQ#14<sup>13</sup> because it already clarified that, "a foreign public fund advised by a banking entity is not considered to be an affiliate of the banking entity so long as the banking entity does not own, control, or hold with the power to vote 25 percent or more of the voting shares of the fund." Any changes must be consistent and adhere to FAQ#14 and related requirements.

## Question 12.

Do the proposed changes to the foreign public fund exclusion, in the aggregate, increase opportunities for evasion of the requirements of section 13? If so, how should the agencies address these concerns? Should the agencies include a specific reservation of authority to prevent evasion through the foreign public fund exclusion, or are the anti-evasion provisions in § \_\_.21 of the implementing regulations sufficient to address these concerns?

It may minimally increase the risk, but given the Rule's proprietary trading provisions have largely been watered down in 2019, don't be a Hypocrite. If the agencies genuinely want to restore public faith in the Rule for proper protection, then re-bring up RENTD and "guilty until proven otherwise" requirements.

## 2. Loan Securitizations

### Question 13.

Does the proposed modification of the loan securitization exclusion sufficiently permit securitization of leases, servicing assets, and related assets, including leases that are security interests? Why or why not? We still think the existing FAQ is sufficient. "Special units of beneficial interest and collateral certificates" pertain to particular commercial interests are something that policy makers should refrain from laying any preferential judgement.

### Question 14.

Should the loan securitization exclusion permit loan securitization issuers to hold a certain percentage of non-loan assets? Why or why not? If so, should the maximum percentage of permissible non-loan assets be five or ten percent, or some other amount? Regardless of the non-loan asset limit, what

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<sup>13</sup> <https://www.federalreserve.gov/supervisionreg/faq.htm#14>



should be the method of calculating compliance with the limit (e.g., market value, par value, principal balance, or some other measure)? Would permitting loan securitization issuers to hold a certain percentage of non-loan assets further the statutory rule of construction in section 13(g)(2) of the BHC Act? If so, explain how.

No, allowing a limited amount of non-loan investments and suggested that permitting such investments would be contrary to the general purpose of section 13 of the BHC Act. Allow me to reemphasize, “the policy objective is to divest the banking system of toxic assets to make banks healthier. The rule and related extension have already considered the practical challenge for a stable run-off of illiquid funds”.

Instead of divesting, banks have the option of converting certain complex investment vehicles from relying on a 1940Act 3(c)7 exemption to, for example, a 3(a)7 exemption. The SEC 3(a)7 exemption “exempts issuers of asset-backed securities the payments on which depend primarily on cash flow from a largely static pool of eligible assets that are not bought and sold for the primary purpose of recognizing gains or losses resulting from market changes.” Such restructuring indeed addresses a bank’s “market risk” and synchronizes with the policy objective. The Rule has been generous instead of pushing for divestment in absolute terms. So, do not attempt to further water down the Rule.

#### **Question 15.**

In what ways, if any, should the agencies limit the type of permissible non-loan assets to certain asset classes or structures (e.g., only debt securities or any permissible asset, such as a derivative)? Would the inclusion of certain financial instruments—such as derivatives and collateralized debt obligations—raise safety and soundness concerns? If so, should qualifying loan securitizations be permitted to hold such instruments and, if so, what restrictions should be placed on the holding of such instruments? What, if any, other restrictions should the agencies impose on non-loan assets to reduce the potential for evasion of the rule?

Enforce the 2013 Rule as it supposed to be rather than tweaking this part of the Rule.

#### **Question 16.**

Should the agencies codify the cash equivalents language in the Loan Securitization Servicing FAQ? Why or why not?

No, please see earlier paragraphs in this section for explanations.

### **3. Public Welfare and Small Business Funds**

#### **Question 17.**

Is the scope of the current public welfare investment fund exclusion properly calibrated? Why or why not? Under what circumstances, if any, have banking entities experienced compliance challenges under Subpart C regarding investments in community development, public welfare, or similar funds that are designed to receive consideration as CRA-qualified investments?



The Public Welfare exemption per Community Reinvestment Act (CRA) does have merits. It may help ease some of the challenges faced by community during this pandemic. Efficiently channeling the fund to the needy is critical. Therefore not all public welfare funds should be exempted. Covenants similar to Federal Grants for non-profit organizations should be observed, and may be capping related total administrative and fund raising costs to less than 20-25%. This is for good course and I encourage the banking industry to strongly support their communities in time of crisis.

### Question 18.

Have banking entities avoided making investments that are designed to receive consideration as CRA-qualified investments because they believed that the investment may not satisfy the public welfare investment fund exclusion? If so, what factors have caused uncertainty as to whether an issuer qualifies for the exclusion for public welfare investment funds?

Way too often banks turned down public welfare project based on Return on Investment (ROI), when banks should have looked at different set of key performance indicators (KPIs), such as program efficiency ratio, administration expense at % of total cost, fundraising efficiency, etc. It's about having the right measurements and gauge appropriate social impacts. Banks ought to reinvigorate their business models for social good in order to regain public confident. After all, banking entity's investment in the fund of funds must "also meet the investment limitations contained in § \_\_.12 of the rule text".

### Question 19.

In what ways would it promote transparency, clarity, and consistency with other Federal banking regulations if the agencies explicitly exclude from the definition of covered fund any issuer that invests exclusively or substantially in investments that are designed to receive consideration as CRA-qualified investments? What policy considerations weigh for or against such an exclusion? What conditions should apply to such an exclusion?

Use KPIs disclosure as I have suggested in respond to Question 18.

### Question 20.

Should the agencies establish a separate exclusion for CRA-qualified investments or incorporate such an exclusion into the exclusion for public welfare investments?

It doesn't matter as long as proper disclosure, capping total administrative and fund raising costs under 20-25%, and consistently "meet the investment limitations contained in § \_\_.12 of the rule text".

### Question 21.

Rural Business Investment Companies (RBICs)—as defined under 203(l) and 203(m) of the Investment Advisers Act of 1940 ("Advisers Act")—are companies licensed under the Rural Business Investment Program (RBIP), a program created as a joint initiative between the U.S. Department of Agriculture and the Small Business Administration. The RBIP was designed to promote economic development and job creation in rural communities by investing in companies involved in the production, processing and





supply of food and agriculture-related products. Under the implementing regulations, are many RBICs excluded from the definition of covered fund because of the public welfare exclusion or because of another provision? Should the agencies provide an express exclusion from the definition of covered fund for RBICs, similar to the exclusion for SBICs? Are RBICs substantially similar to SBICs and public welfare companies that banking entities are permitted to make and retain investments in under section 13(d)(1)(E) of the BHC Act? Would excluding RBICs in the same manner that SBICs and public welfare companies are excluded from the definition of covered fund provide certainty regarding the covered fund status of RBICs or serve similar interests, as identified by commenters in response to the 2018 proposal?

We still have reservation about SBIC exclusion. Volcker Rule never prohibits banks from direct lending to small businesses. Why should there be frequent buying and selling of these SBIC funds? If banks only act as sponsors while incapable to lend directly to small businesses, does the economy still need banks to seat in the middle<sup>14</sup>? I assume the same should apply to RBICs. Therefore, it is about extending loans, not “speculating” on SBIC or other funds.

#### **Question 22.**

The Tax Cuts and Jobs Act established the “opportunity zone” program to provide tax incentives for long-term investing in designated economically distressed communities. The program allows taxpayers to defer and reduce taxes on capital gains by reinvesting gains in “qualified opportunity funds” (QOFs) that are required to have at least 90 percent of their assets in designated low-income zones. Do commenters believe that many or all QOFs are excluded from the definition of covered fund under the implementing regulations under the public welfare exclusion or another exclusion or exemption? Should the agencies provide an express exclusion from the definition of covered fund for QOFs? Are QOFs substantially similar to SBICs and public welfare companies that banking entities are permitted to make and retain investments in under section 13(d)(1)(E) of the BHC Act? Would excluding QOFs in the same manner that SBICs and public welfare companies are excluded from the definition of covered fund provide certainty regarding the covered fund status of QOFs or serve similar interests, as identified by commenters in response to the 2018 proposal?

If meeting the 249.10(c)(11) requirements, then QOF could have used exemption currently available. “Carve out” of a separate exclusion is NOT recommended.

#### **Question 23.**

Should the agencies revise the SBIC exclusion as proposed? Why or why not? Would the proposed revisions to the SBIC exclusion appropriately address issuers that surrender their SBIC licenses? If not, what changes should be made to the proposal?

No. “Surrender license” doesn't necessary mean the small business has prospered, it could also be failure, or simply not meeting (or not wanting to comply) with SBA.gov criteria. This is a commercial

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<sup>14</sup> <https://psmag.com/economics/banks-dont-much-banking-anymore-thats-serious-problem-72654>





decision on the bank side to seek exit strategy. Volcker Rule is in no position to skew regulatory policy to ensure commercial profitability. The agencies' proposal does not address this legitimate concern I raised since 2018. Volcker Rule never prohibits banks from direct lending to small businesses. Why should there be frequent buying and selling of these SBIC funds? If banks only act as sponsors while incapable to lend directly to small businesses, does the economy still need banks to seat in the middle<sup>14</sup>?!

**Question 24.**

Should the proposed exclusion for issuers that surrender their SBIC licenses include a requirement that the issuer operate pursuant to a written plan to dissolve within a set period of time, such as five years?

Why or why not? If so, what is the appropriate time period?

No, please see my responds to Question 23 for explanations.

**Question 25.**

What additional restrictions, if any, should apply to the proposed exclusion for issuers that surrender their SBIC licenses?

Please see my responds to Question 23.

**Question 26.**

What specific activities or investments, if any, should an issuer that surrenders its SBIC license be expressly permitted to engage in during wind-down phases, such as follow-on investments in existing portfolio companies and why? What conditions should apply to such activities or investments?

Please see my responds to Question 23.



## C.) Proposed Additional Covered Fund Exclusions

### 1. Credit Funds

This is tricky because prevailing market turmoil does call for life-line support in extending credits. Yet, the original preamble to the 2013 rule validly stated the concerns that such “credit funds” could be private equity funds and hedge funds and the possible evasion of the requirements of section 13 of the BHC Act “if” credit fund exclusion is to be granted. We still lean toward relying on the joint venture and loan securitization exclusions instead of a separate “carve-out” for “credit funds”.

If banking entities cannot restructure and re-bundle these products to fit the joint venture and loan securitization exclusions’ requirements, then it is probably too illiquid or toxic, or among which the related exposures to warrants/ interest rate/ foreign exchange derivatives are unacceptable or too much like a speculative investments in private equity funds and hedge funds.

We respect the agencies attempt to add additional restrictions to ensure that the issuer is actually engaged in providing credit and credit intermediation and is not operated for the purpose of evading the provisions of section 13 of the BHC Act. However, if banks only act as sponsors/ investors/ speculative traders of “Credit Funds” while incapable to lend directly, does the economy still need banks to seat in the middle<sup>14</sup>?!

#### Question 27.

Is the proposed rule’s approach to a credit fund exclusion appropriate and effective? Why or why not?

Do the conditions imposed on the proposed exclusion effectively address the concerns about administrability and evasion that the agencies expressed in the preamble to the 2013 rule?

No, please see earlier paragraphs in this section for explanations.

#### Question 28.

What types of loans and permissible debt instruments or some subset of those assets, if any, should a credit fund be able to hold? Are the definitions used in the proposed exclusion appropriate and clear?

It is better for banks to restructure and re-bundle suitable assets to fit the joint venture and loan securitization exclusions’ requirements, rather than “carve out” a separate “credit fund” exclusion because this could be an uncontrollable backdoor to PEFs and HFs speculations. There are way too many related exposures to warrants, interest rate, foreign exchange derivatives mixed into so called “credit funds” that no rule can possibly list them all but has to be reviewed on a case by case basis. Please see earlier paragraphs in this section for elaborated explanations.

#### Question 29.

The agencies believe it could be appropriate to permit credit funds to hold a small amount of non-loan and non-debt assets, such as warrants or other equity-like interests directly related to the other



permitted assets, subject to appropriate conditions. Should credit funds be able to hold small amounts of equity securities (or rights to acquire equity securities) received on customary terms in connection with the credit fund's loans or debt instruments? If so, what should be the quantitative limit on permissible non-loan and non-debt assets? Should the limit be five or ten percent of assets, or some other amount? How should such quantitative limit be calculated? Does the holding of a certain amount of equity securities (or rights to acquire equity securities) raise concerns that banking entities may use credit funds to evade the limitations and prohibitions in section 13 of the BHC Act? Why or why not? For example, under the proposal, could the holdings of an excluded fund be predominantly equity securities (or rights to acquire equity securities) received on customary terms in connection with the credit fund's loans or debt instruments? If so, how?

No. We object any amount of non-loan investments and there should be no separate "carve out" of "credit funds" exclusion. Permitting such investments would be contrary to the general purpose of section 13 of the BHC Act (i.e. to divest banking entities of risky assets). Joint venture and loan securitization exclusions are sufficient to permit reasonable activities. We understand it may be difficult to off-load these non-loan exposures during this market turmoil where liquidity evaporated. There can be temporary relief to defer a stable run-off of these assets, but this backdoor cannot be opened or else it would exacerbate volatility in market and/or fundamentally contrary to the purpose of Volcker Rule about divesting risky assets. Please see earlier paragraphs in this section for elaborated discussion.

#### **Question 30.**

The proposed credit fund exclusion would permit excluded credit funds to hold related rights and other assets that are related or incidental to acquiring, holding, servicing, or selling loans or debt instruments, provided that each right or asset that is a security meets certain requirements. Should credit funds be allowed to hold such related rights and other assets? Are these assets necessary for the proper functioning of a credit fund? Are the requirements regarding rights or assets that are securities applicable to the holdings of credit funds or otherwise appropriate?

No, please see earlier paragraphs in this section for explanations.

#### **Question 31.**

Is the list of permitted securities appropriately scoped, overbroad, or under-inclusive? Why or why not? Should the list of permitted securities be modified? If so, how and why?

No, please see our respond to Question 28 and earlier paragraphs in this section for explanations.

#### **Question 32.**

The proposal provides that any interest rate or foreign exchange derivatives held by the credit fund adhere to certain requirements. Should credit funds be allowed to hold these, or any other type of derivatives? Are the requirements that the written terms of the derivatives directly relate to assets held and that the derivatives reduce the interest rate and/or foreign exchange risks related to the assets held



applicable to the holdings of credit funds generally? Are such requirements otherwise appropriate? Why or why not?

No, please see our respond to Question 28 and earlier paragraphs in this section for explanations.

#### **Question 33.**

Which safety and soundness standards, if any, should be referenced in the credit fund exclusion? Should the agencies reference the safety and soundness standards codified in the banking agencies' regulations, e.g., 12 CFR part 30, 12 CFR part 364, or other safety and soundness standards? Safety and soundness standards can vary depending on the type of banking entity. Is there a universally applicable standard that would be more appropriate, such as standards applicable to insured depository institutions?

This backdoor should NOT be opened. Please see our respond to Question 28 and earlier paragraphs in this section for explanations.

#### **Question 34.**

Is the application of sections \_\_.14 and \_\_.15 to the proposed credit fund exclusion appropriate? Why or why not? Should a banking entity that sponsors or serves as an investment adviser to a credit fund be required to comply with the limitations imposed by both sections \_\_.14(a) and (b)? Why or why not? Please see earlier paragraphs in this section that explains our objection to "carve out" credit fund exclusion. Again, banks should rely on joint venture and loan securitization exclusions as fit.

#### **Question 35.**

Is it appropriate to require a banking entity that sponsors or serves as an investment adviser or commodity trading advisor to a credit fund, to comply with the disclosure requirements of § \_\_.11(a)(8), as if the credit fund were a covered fund? Why or why not?

Please see earlier paragraphs in this section that explains our objection to "carve out" credit fund exclusion. Again, banks should rely on joint venture and loan securitization exclusions as fit.

#### **Question 36.**

Is the definition of proprietary trading in the credit fund exclusion appropriately scoped, overbroad, or under-inclusive? Why or why not? If the definition is not appropriately scoped, is there an alternative definition of proprietary trading? Should credit funds sponsored by, or that have as an investment adviser, a banking entity be able or be required to use the associated banking entity's definition of proprietary trading, for the purposes of this exclusion? Why or why not? Would such an approach impose undue compliance burdens? If so, what are such burdens?

Overboard/ under-inclusive, or no matter how the agencies attempt to articulate the definition, the trouble is: this backdoor cannot reasonably be controlled once opened. Please see earlier paragraphs in this section that explains our objection to "carve out" credit fund exclusion. Again, banks should rely on joint venture and loan securitization exclusions as fit.



**Question 37.**

Should the agencies establish additional provisions to prevent evasion of section 13 of the BHC Act? Why or why not? If so, what requirements would be appropriate and properly balance providing firms with flexibility to facilitate extensions of credit and ensuring compliance with section 13 of the BHC Act? For example, should the agencies impose quantitative limitations, additional capital charges, control restrictions, or other requirements on use of the credit fund exclusion? Banks should rely on joint venture and loan securitization exclusions as fit. Please see earlier paragraphs in this section that explains our objection to “carve out” credit fund exclusion.

**Question 38.**

The proposed exclusion for credit funds is similar to the current exclusion for loan securitizations. Should the agencies combine the proposed credit fund exclusion with the current loan securitization exclusion? If so, how? What would be the benefits and drawbacks of combining the exclusions or maintaining separate exclusions for each type of activity? If the two exclusions remain separate, should the proposed credit fund exclusion contain a requirement that a credit fund not issue asset-backed securities? Why or why not?

Please do not attempt to permanently water down this part of the Rule by hiding credit funds under the guise of loan securitizations when certain funds do not meet the set criteria. We object any slick way to create backdoor that contrary to the Volcker Rule’s divestment of risky assets objective. That being said, we are okay if the agencies would consider a deferral for a stable run-off of these credit funds and/or use “Stress RENTD” to provide a temporary relief amid the current financial turmoil.

## **2. Venture Capital Funds**

We fully respect the SEC’s definition that helps to distinguish the investment activities of venture capital funds from those of hedge funds and private equity funds. However, we disagree that the risk in investing in venture capital funds is necessarily any less than PEFs or HFs, because the emphasis is about the manner of speculative bets that may constitute as Volcker violation, not necessarily the risk of the investment vehicle per se (obviously stable run-off of toxic assets is also one of the Rule’s objectives).

Another concern we have is the competitiveness of public market versus private market. Per my submitted comments<sup>15</sup> to the SEC in Dec 2019, angel funding, private equities and venture capitals, have the advantages of being an informed group and often with board connectivity to exert influence on management. So, they provide both money and skills to effectively unleash values in small companies. However, they have higher funding cost and Main Street American investors could possibly miss out on stock appreciation opportunities when private equity and venture capital are overly competitive with

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<sup>15</sup> <https://www.sec.gov/comments/s7-18-19/s71819-6555835-200936.pdf>





the public market<sup>16</sup>. Therefore, appropriate balancing between the public market and private market is needed.

The collapse of Long-Term Capital Management (LTCM)<sup>17</sup> in 1998 posed widespread concern about systemic risk if a hedge fund failure led to the failure of its counterparties. Although the former Federal Reserve Board Chairman – Ben Bernanke once said he "would not think that any hedge fund or private equity fund would become a systemically critical firm individually",<sup>18</sup> herd behavior and extensive use of leverage can cause a number of HFs, PEFs, and the like businesses (such as Venture Capital Funds), to make substantial losses/ forced liquidations at the same time. Domino effects exacerbate into crisis through their interconnection with prime brokers. European Central Bank has charged that hedge funds pose systemic risks to the financial sector.<sup>19</sup>

Following table highlighted synergies between HFs, PEFs, Venture Capital Funds and banks, while contrasted it for implications when such synergies are abused.

Synergies between HFs/ PEFs/ VCFs and banks	If and when 'Economy of Scope' <sup>20</sup> is abused
HFs/ PEFs/ VCFs provide better returns for banks than processing clients' transactions/ other traditional services	Deviate from banks' traditional role to transform liquidity and maturity, short-term orientation, induce volatility, increase susceptibility to stress
Banks provide source of cheap funding to HFs/ PEFs/ VCFs that boosts competitiveness (via less leverage, or can double-down with favorable margins to leverage up for more aggressive strategies)	Had power of mass destruction – small exploitations turned into outsized bets/ bubbles, proliferate by bets on others' bets, exacerbate into an arena of passing problems on down the line until the system itself collapsed.
Prime brokerage as match makers between clients and managers, dark-pool internalization, and other back-office supports	Potential conflict of interest (information advantage/ order routing issue), <sup>21</sup> central counterparty risk, clustering, contagious to become liquidity crunch
Off-load non-performing assets via less-transparent HF/ PEF/ VCF channels; more varieties to hedge/ manage liquidity for hard-to-value assets, and make market for thinly traded instruments	Stuck with the illiquid, reflate of toxic, speculate instead of assets-liabilities management hedges, <b>Error! bookmark not defined.</b> risks non-transferrable when correlation breaks, derivative contracts are hard to untangle, nurture gambling/ game of controls to cover losses

Policy makers ought to consider where the economy of scope may have abuses when they are combined, but won't cause undue hardship to society when they are run separately. Delineation of

<sup>16</sup> <https://www.linkedin.com/pulse/missed-opportunities-average-investors-kelvin-to/>

<sup>17</sup> Greenspan, Alan (2007). *The Age of Turbulence: Adventures in a New World*. The Penguin Press. pp. 193–195. ISBN 978-1-59420-131-8.

<sup>18</sup> <http://www.gpo.gov/fdsys/pkg/CHRG-111hhrg55809/pdf/CHRG-111hhrg55809.pdf>

<sup>19</sup> <http://www.ecb.int/pub/pdf/other/financialstabilityreview200606en.pdf>

<sup>20</sup> <https://www.investopedia.com/terms/e/economiesofscope.asp>

<sup>21</sup> [https://www.thetradenews.com/baml-slapped-second-time-42-million-fine-masking-orders/;](https://www.thetradenews.com/baml-slapped-second-time-42-million-fine-masking-orders/)

<https://www.bloomberg.com/news/articles/2018-09-14/citigroup-pays-almost-13-million-to-settle-sec-dark-pool-probe>



rights is different from incorporating a definition or articulating the terminology differences between Venture Capital Funds and PEFs/HFs. I believe clues/analogy to solve this regulatory reform challenge can be found in "*The Theory of Share Tenancy*"<sup>22</sup> by Economic Guru – Stephen N.S. Cheung, PhD. I will be glad to discuss further specifics with the regulators, industry groups, and banks, and/or testify in front of Congress upon request.

Given the various reasons above, we object "carving out" Venture Capital Fund exclusion.

**Question 39.**

Is the proposed exclusion for qualifying venture capital funds appropriate? Why or why not?

No, please see earlier paragraphs in this section for explanations.

**Question 40.**

Does the proposed exclusion for qualifying venture capital funds include the appropriate vehicles? Why or why not? If not, how should the agencies expand or narrow the vehicles for which banking entities would be permitted to make use of the exclusion? What modifications to the proposed exclusion would be appropriate and why?

No, the emphasis is about the manner of speculative bet, not necessarily the risk of the investment vehicle per se. Please see earlier paragraphs in this section for explanations.

**Question 41.**

Are the proposed conditions on the proposed exclusion for qualifying venture capital funds appropriate? Why or why not? If not appropriate, how should the agencies modify the conditions, and why?

No, please see earlier paragraphs in this section for explanations.

**Question 42.**

Would permitting banking entities to invest in or sponsor a qualifying venture capital fund promote and protect the safety and soundness of banking entities and the financial stability of the United States?

What data is available to support an argument that venture capital funds would or would not promote and protect the safety and soundness of banking entities and the financial stability of the United States?

Safety and soundness are promoted by advancing control practices, not by "carving out" new exclusion to relax the Rule. Please see earlier paragraphs in this section for explanations.

**Question 43.**

Are the requirements for a qualifying venture capital fund sufficient to distinguish these types of funds from covered funds? Are there any additional standards or requirements that should apply to a qualifying venture capital fund? If so, what are they and why should they apply?

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<sup>22</sup> <https://www.journals.uchicago.edu/doi/pdfplus/10.1086/259477>





Distinguishing it is one thing; it is another matter if the financial institution's trading activities, investment interests and relationships with venture capital funds are "qualified" under appropriate exemptions. Please see earlier paragraphs in this section for explanations.

**Question 44.**

Should the additional proposed revenue requirement be added to the venture capital fund exclusion to help ensure that the investments made by excluded venture capital funds are truly made in small and early-stage companies? Why or why not? If the additional restriction is added, is \$50 million an appropriate annual revenue limit? If not, what would be an appropriate revenue limit? Is there a metric other than annual gross revenue, such as amount of time in operation, that would serve as a better indicator of whether an investment in a company should allow a venture capital fund to qualify for the exclusion?

\$50 million revenue or other threshold is merely a matter of commercial interest of who is allowed to be in the game; policy maker should preserve their independence and refrain from laying any preferential treatment. Again, we object "carving out" Venture Capital Fund exclusion. Please see earlier paragraphs in this section for explanations.

**Question 45.**

Should the proposed venture capital fund exclusion require that 100 percent of the fund's holdings, other than short-term holdings, be in qualifying investments instead of the 80 percent that is required under 17 CFR 275.203(l)-1(a)(2)? Why or why not?

80% or 100%, short or long-term holding ... these are all very subjective and may constantly change, especially for private market investment vehicles. This is unlike the transparency level of investments in the public market. Again, we object "carving out" Venture Capital Fund exclusion. Please see earlier paragraphs in this section for explanations.

**Question 46.**

Are there provisions or conditions of the definition under rule 203(l)-1 under the Advisers Act that are inappropriate for purposes of determining an exclusion from the "covered fund" definition in § \_\_\_.10? If so, please explain why the purposes of an exclusion from the "covered fund" definition should lead the agencies to exclude a provision or condition, such as paragraph (a)(2), of the definition under rule 203(l)-1 under the Advisers Act.

There is nothing wrong with the definition under rule 203(l)-1 under the Advisers Act. It is the manner of speculation or possibility of exploitation if abusing the economy of scope when combined with bank business. Again, we object "carving out" Venture Capital Fund exclusion. Please see earlier paragraphs in this section for explanations.



**Question 47.**

How would a banking entity ensure the activities of a qualifying venture capital fund are consistent with the safety and soundness standards that apply to the banking entity? Are the standards and requirements for a banking entity that acts as a sponsor, investment adviser, or commodity trading advisor to a qualifying venture capital fund appropriate to apply to a qualifying venture capital fund? Are there any additional standards or requirements that should apply to a banking entity that acts as a sponsor, investment adviser, or commodity trading advisor to a qualifying venture capital fund? If so, what are they, and why should they apply?

Safety and soundness are promoted by advancing control practices, not by “carving out” new exclusion to relax the Rule. Please see earlier paragraphs in this section for explanations.

**Question 48.**

A banking entity that sponsors or advises a qualifying venture capital fund would be required to comply with the limitations imposed by sections \_\_.14 (except the banking entity may acquire and retain any ownership interest in the issuer) and \_\_.15 of the 2013 rule, as if the qualifying venture capital fund were a covered fund. Is the application of these sections to the proposed venture capital fund exclusion appropriate? Why or why not?

Good try, but no. Our objection is also about striking appropriate balance between public versus private market, please see earlier paragraphs in this section for explanations.

**Question 49.**

Is it sufficiently clear what kind of assets or investments would result in a conflict of interest or an exposure to a high-risk asset or high-risk trading strategy in the context of a qualifying venture capital fund? Should the agencies provide additional parameters regarding the types of assets and strategies that could result in such exposure in this context?

Conflict of interest cannot reasonably be assessed by one claiming their own compliance with the Rule, but via in-depth study of consistency of actual practices and meeting other criteria using a line-by-line item review for proper assurance. Without corresponding enforcement mechanism, whatever assertion of no conflict exists would merely be hypes benefiting big law/ consulting firms. Again, it is not the kind of assets or investments being evil, it's the act of speculation or exploitative behaviors that the Rule aims to curb. Just like the Rule does not prohibit derivatives or loan securitization as an asset class, but the inappropriate “use” of derivatives or securitization could be potential Volcker violation.

**Question 50.**

Should the agencies exclude from the definition of covered fund, or otherwise permit the activities of, certain long-term investment funds that would not be qualifying venture capital funds? For example, should the agencies provide an exclusion for issuers (1) that make long-term investments that a banking entity could make directly, (2) that hold themselves out as entities or arrangements that make investments that they intend to hold for a set minimum time period, such as two years, (3) whose



relevant offering and governing documents reflect a long-term investment strategy, and (4) that meet all other requirements of the proposed qualifying venture capital fund exclusion (other than that the issuers would be venture capital funds as defined in 17 CFR § 275.203(l)-1)? Would the rationale for excluding qualifying venture capital funds also extend to such long-term investment funds? Why or why not? If the agencies were to adopt an exclusion for long-term investment funds, should the agencies impose safeguards on such an exclusion? If so, what safeguards should the agencies impose, and why? Would such an exclusion promote and protect the safety and soundness of the banking entity and the financial stability of the United States? If so, how?

As much as I like to think long-term investment should be rewarded and supported generally over any short-term speculations, yet the agencies do not provide concrete examples of what these “other than” Venture Capital funds might be. Hence, we can only oppose it because the scope can be way too board.

#### **Question 51.**

Is there evidence that the covered fund provisions have caused banking entities to make more standalone direct balance sheet investments? If so, have these investments increased or decreased risk to banking entities?

Venture Capital Funds are profitable source of revenues for banks. Given that all profitable businesses come with risks, unless policy makers or others provide any explicit or implicit guarantee(s). In fact, policy makers should refrain from skewing market structure to favor particular group of players. Given that, the more appropriate question should be: are the risks acceptable? And the answer is: it depends. When everything is rosy, there would be no problem; but during the current market turmoil, the risk is especially high. Hence, we do not recommend “carving out” Venture Capital Fund exclusion. Please see earlier paragraphs in this section for elaborated discussion.

#### **Question 52.**

Is there evidence that the covered fund provisions have negatively impacted the provision of financing? If so, is this impact non-uniform? For example, are effects more acute in certain geographic areas or in certain industries? To the extent negative effects are asymmetric by geography or otherwise, would the proposal effectively address these asymmetries? Is there evidence that the covered fund provisions have caused end-users to seek financing from non-banking entities? If so, would the proposed exclusion for qualifying venture capital funds help to address these impacts?

Yes and No, depends on type of financing activities. The comprehensiveness of covered fund provision is effective to push banks to decisively exit hedge funds (HFs) and private equity funds (PEFs) and the like businesses (such as Venture Capital Funds), while drying of liquidities are also caused by partially by impending market structure problems<sup>23</sup> and partially due to poor quality of investments. Unfortunately, venture capital funds exclusion for banks would not help improve the situation because: (1) banks largely exited this market; (2) it will exacerbate the private versus public market competitiveness issue

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<sup>23</sup> <https://www.sec.gov/news/speech/clayton-redfearn-equity-market-structure-2019>



that cause main street investors to miss out opportunities; (3) the current market turmoil makes it especially risky and we don't want to use banks' or taxpayers' money to bail out the venture capitals during crunch time.

### 3. Family Wealth Management Vehicles

We opposed "carve out" of a family wealth management exclusion per our respond<sup>3</sup> in 2018, while citing certain controversial aspects regarding Congress indeed recognized family offices are not within the sphere of investment advisers intended to be covered by the Advisers Act, while "family wealth management vehicles" may utilize identical structures and pursue comparable investment strategies that are hard to distinguish from a hedge fund or private equity fund. Despite a 'ten-generation limit' on "family members" under 202(a)(11)(G)-1 is helpful to determine scope of related family members a family office wishes to serve, but the limit does not represent 'ownership interest' or 'control' over the fund. Therefore, our 2018 recommendation suggests the agencies to use discretion to consider a "no-action relief" on case-by-case basis.

Our 2018 recommendation was under the condition that the family wealth management vehicle must meet the various requirements prescribed by the Agencies, "plus" (i) majority of a family office's board of directors to be family members that hold controlling ownership stake in the fund; and (ii) curb any restructure of fund, redemption, or assignment of rights that evade the restrictions of section 13 on covered fund activities.

As times go by, not sure how many successful cases that banks are able to rely on the 248.10(d)(2) cash collateral pools exclusion to get their wealth management vehicles to meet the requirement of sections 3(c)(1) and 3(c)(7) of the 40 Act, or to operate pools as separate accounts to exclude from the covered fund definition. We hope the agencies and other commenters can show some statistics. Anyway, if the agencies' experience is leaning toward making this "family wealth management" a separate exclusion, then please at least add the 2 stated conditions - (i) majority of a family office's board of directors to be family members that hold controlling ownership stake in the fund; and (ii) curb any restructure of fund, redemption, or assignment of rights that evade the restrictions of section 13 on covered fund activities on top of the agencies' proposed requirements of (1) if organized as a trust, the grantor(s) of the entity are all family customers and, (2) if not organized as a trust, a majority of the voting interests in the entity are owned (directly or indirectly) by family customers; and the entity is owned only by family customers and up to 3 closely related persons of the family customers.

#### Question 53.

Should the agencies exclude family wealth management vehicles from the definition of "covered fund" as proposed? Does the agencies' proposed definition of "family wealth management vehicle" include the appropriate vehicles? What, if any, modifications to the scope, definitions or conditions prescribed



in the proposed exclusion should be made? Should the agencies provide any additional guidance or requirements regarding the conditions? For example, should the agencies provide additional guidance or requirements regarding the timing of the disclosures required by § \_\_.11(a)(8)?

Under conditions as stated in earlier paragraphs of this section.

**Question 54.**

Would an exclusion for family wealth management vehicles create any opportunities for evasion, for example, by allowing a banking entity to structure investment vehicles to evade the restrictions of section 13 on covered fund activities? Why or why not? If so, how could such concerns be addressed? Please explain.

Yes, please refer to earlier paragraphs in this section for explanations.

**Question 55.**

Are there alternative approaches the agencies should take to enable banking entities to provide family wealth management vehicles with banking and asset management services?

Currently, there is the 248.10(d)(2) exclusion. Family wealth management vehicles, such as Cash Collateral Pools (CCP) may rely on sections 3(c)(1) and 3(c)(7) of the 40 Act to avoid being an Investment Company (IC). If registered CCP with the SEC as IC, then they may operate pools as separate accounts to exclude from the covered fund definition.

**Question 56.**

The proposed exclusion would require the banking entity and its affiliates to comply with the requirements of 12 CFR 223.15(a), as if such banking entity and its affiliates were a member bank and the issuer were an affiliate thereof. Should the agencies adopt this proposed requirement? Why or why not? Would this proposed requirement address the agencies' concerns about banking entities or their affiliates bailing out a family wealth management vehicle? Why or why not?

Yes. 12 CFR 223.15(a) stated that "A member bank may not purchase a low-quality asset from an affiliate unless, pursuant to an independent credit evaluation, the member bank had committed itself to purchase the asset before the time the asset was acquired by the affiliate." This seems prudent, and there are additional requirements we recommend if a separate "carve out" of wealth management exclusion is to be permitted by the agencies. Please see earlier paragraphs in this section for explanations.

**Question 57.**

The proposed exclusion permits ownership of the family wealth management vehicle by 3 closely related persons of the family customer owners. Should the exclusion permit closely related persons to invest in family wealth management vehicles? What, if any, modifications should the agencies make to the proposed definition of "closely related person"? Why or why not? For example, should the definition of "closely related person" include individuals with longstanding personal relationships with





family customers, but exclude individuals with only longstanding business relationships with family customers, or vice versa? Should the number of closely related persons permitted to invest in the family wealth management vehicle be increased, decreased, or remain at 3 such persons? Should, for example, the agencies consider raising the number of closely related persons to 10 to parallel the number of permitted unaffiliated co-venturers permitted under the § \_\_.10(c) exclusion for joint ventures? Why or why not? What if any other or additional qualitative or quantitative limits on the ownership interest of closely related persons in family wealth management vehicles? Would the inclusion of closely related persons that are not family customers in the family wealth management vehicle exclusion raise concerns about these vehicles being used to evade the prohibitions in section 13 of the BHC Act? Why or why not? Commenters should offer specific examples detailing when it would be appropriate for a family wealth management vehicle to include persons that are not family customers.

Given a 'ten-generation limit' on "family members" under 202(a)(11)(G)-1 is helpful to determine scope of related family members a family office wishes to serve, but the limit does not represent 'ownership interest' or 'control' over the fund, so this is a moot point. That's why we think the agencies should also review if "majority of a family office's board of directors to be family members that hold controlling ownership stake in the fund".

#### **Question 58.**

The proposed family wealth management vehicle exclusion would permit a banking entity or its affiliates to hold up to 0.5 percent of the issuer's outstanding ownership interests only to the extent necessary for establishing corporate separateness or addressing bankruptcy, insolvency, or similar concerns. Instead of permitting such an ownership interest to be held by a banking entity or its affiliates, should the agencies permit such an ownership interest to be held by a third party that is unaffiliated with either the banking entity or the family customer? Why or why not?

"Ownership interest to be held by a third party" may indeed only benefit those law/ consulting firms, a fixed percentage seems more clear cut.

#### **Question 59.**

The proposed family wealth management vehicle exclusion would require the banking entity and its affiliates to comply with the requirements of § \_\_.14(b) and § \_\_.15 , as if the family wealth management vehicle were a covered fund. Should the exclusion require also that the banking entity and its affiliates comply with the requirements of all of § \_\_.14? Why or why not?

I tend to think operating pools as separate accounts to exclude from the covered fund definition would probably be a better choice for many than using this proposed wealth management exclusion. So, why go through the hassle when workarounds are available to offer adequate relief.



## 4. Customer Facilitation

We have seen submitted comments by industry lobbyists in 2018 using “customer-facing”, or the like (e.g. loan related swaps loan level hedging, matched book trading, customer-driven derivatives) as arguments to push for lifting related proprietary trading ban requirements. Yet, please be reminded that if the transaction is dealing with “customers”, following conditions must be met:

- fiduciary capacity for a customer
- transaction is conducted for the account of, or on behalf of customer
- banking entity does not have or retain beneficial ownership of the instruments
- riskless principal

If the transaction is dealing with “counterparty”, §\_.5(b) risk-mitigating hedge exemption may be used if meeting the following requirements:

- §\_.5(b)(1)(ii) “... on-going monitoring...,”
- (iii) “... independent testing... such correlation analysis demonstrates ...,”
- (2)(ii) “At the inception of the hedging activities...,”
- (iv)(C) “Requires ongoing recalibration.”

Unfortunately, §\_.5(b) requirements have been weakened per 2019 revision<sup>5</sup>. I am not sure how the agencies are going to curb banks luring customers into illiquid, complex, and hard to untangle derivative contracts that possibly violate banks' fiduciary responsibilities. Also, how regulators plan on scrutinizing banks' possible attempts to flip-switch between dealing with “client” versus “counterparty”? Price risk shifted to upstream banks, but banks don't necessarily have a better way to manage it. Yet, it gives rise to credit and liquidity risks that can possibly become systemic risk to the overall financial system. New risk may be introduced in the process of reducing price risk. Are banks cautiously entering into hedges instead of constant flipping between buy/ sell hedges? These questions remain unanswered in the agencies' 2020 proposal.

That being said, as a former bank executive and championed in customer fulfillment, I do like to see banks growing their customer supports. Therefore, it is a matter of balancing the right controls with fulfillment of customer needs. I do see the SEC suggested risk mitigation approach as reasonable (i.e. imposing conditions, such as: (1) banking entity and its affiliates can hold only up to 0.5% interest in the customer facilitation vehicle for the purpose of and to the extent necessary for establishing corporate separateness or addressing bankruptcy, insolvency, or similar concern; (2) not directly or indirectly guarantee, assume, or otherwise insure the obligations or performance of the vehicle.)

In my opinion, the relief should be limited to authorizing banking entities to engage “only” in extensions of intraday credit, payment, clearing, and settlement services, with covered funds for operational efficiency purposes, but nothing more. Whether banking entities choose to outsource such potential permissible activities to third parties is a commercial decision, and the agencies should refrain from skewing policies in favor of any particular groups.





**Question 60.**

Is the proposed exclusion for customer facilitation vehicles appropriate? Why or why not?

Can be, if the agencies can clarify and push for advancement of controls to monitor possible flipping of the switch between “customers” versus “counterparties”, plus add another condition to permit “only” the following activities: extensions of intraday credit, payment, clearing, and settlement services, with covered funds for operational efficiency purposes.

**Question 61.**

Does the proposed exclusion for customer facilitation vehicles include the appropriate vehicles? Why or why not? If not, how should the agencies expand or narrow the vehicles for which banking entities would be permitted to make use of the exclusion? What modifications to the proposed exclusion would be appropriate and why?

I don’t know how many times I have to repeat over and over again – the emphasis is about the manner of speculative bet, not necessarily the risk of the investment vehicle per se.

**Question 62.**

Are the proposed conditions on the proposed exclusion for customer facilitation vehicles appropriate? Why or why not? If not appropriate, how should the agencies modify the conditions, and why?

Please see respond to Question 60 and earlier paragraphs in this section.

**Question 63.**

Should the agencies require, as a condition for satisfying the proposed exclusion, that the customer facilitation vehicle be formed at the request of the customer? Why or why not?

We all know what “anticipation of customer demand” really means and how much water that definition may hold; please don’t be slick.

**Question 64.**

Should the agencies specify to which types of transaction, investment strategy, or other service such a customer facilitation vehicle could be formed to facilitate exposure? Why or why not?

“Only” the following activities: extensions of intraday credit, payment, clearing, and settlement services, with covered funds and it had to be “for operational efficiency purposes”.

**Question 65.**

The proposed exclusion would permit a banking entity or its affiliates to hold up to 0.5 percent of the issuer’s outstanding ownership interests only to the extent necessary for establishing corporate separateness or addressing bankruptcy, insolvency, or similar concerns. Instead of permitting such an ownership interest to be held by a banking entity or its affiliates, should the agencies permit such an ownership interest to be held by a third party that is unaffiliated with either the banking entity or the customer? Why or why not?



“Ownership interest to be held by a third party” may indeed only benefit those law/ consulting firms, a fixed percentage seems more clear cut.

#### Question 66.

The proposed exclusion would require the banking entity and its affiliates to comply with the requirements of § \_\_.14(b) and § \_\_.15 , as if the customer facilitation vehicle were a covered fund. Should the exclusion require also that the banking entity and its affiliates comply with the requirements of all of § \_\_.14? Why or why not?

Bottom line, banking entities should use other existing exclusions rather than this, because the \$6.2 billion loss in the 2012 JPMC case taught us important lessons<sup>24</sup>, such as: “Increased risk without notice to regulators, Mischaracterized high risk trading as hedging, Hid massive losses, Disregarded risk, Dodged regulatory oversight, Mischaracterized the portfolio, etc.”

#### Question 67.

The proposed exclusion would require the banking entity and its affiliates to comply with the requirements of 12 CFR 223.15(a), as if such banking entity and its affiliates were a member bank and the issuer were an affiliate thereof. Should the agencies adopt this proposed requirement? Why or why not? Would this proposed requirement address the agencies’ concerns about banking entities or their affiliates bailing out a customer facilitation vehicle? Why or why not?

Think about why the agencies have reservations about complying with the requirements of 12 CFR 223.15(a), then you may imagine how convoluted this so called “customer facilitation” exclusion can be.

#### Question 68.

Would the proposed exclusion for customer facilitation vehicles create any opportunities for evasion, for example, by allowing a banking entity to structure such vehicles in a manner to evade the restrictions of section 13 on covered fund activities? Why or why not? If so, what conditions could be imposed to address such concerns? For example, should the agencies impose a restriction that a customer facilitation vehicle only be able to serve customers who initiate or request a given transaction, investment strategy, or other service? Do the conditions that would be imposed on the proposed exclusion address those concerns? Please explain.

See respond to Question 60 and earlier paragraphs in this section for additional suggested conditions.

#### Question 69.

Should the agencies take a different approach to enable banking entities to provide customers with exposure to a transaction, investment strategy, or other service provided by the banking entity? For example, would modifications to § \_\_.14 of the implementing regulations, whether as proposed below or otherwise, allow banking entities to provide customers with this exposure? Please explain.

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<sup>24</sup> <https://www.hsgac.senate.gov/subcommittees/investigations/hearings/chase-whale-trades-a-case-history-of-derivatives-risks-and-abuses>



The agencies should curb any acts that banks may potentially lure customers into illiquid, complex, and hard to untangle derivative contracts that possibly violate banks' fiduciary responsibilities.

**Question 70.**

For banking entities with significant trading assets and liabilities that sponsor funds relying on the proposed exclusion for customer facilitation vehicles, would it be appropriate to require additional documentation requirements pursuant to § \_\_.20(e)(2) consistent with other sponsored funds relying on certain exclusions from the definition of covered fund? Why or why not? Similarly, should the documentation requirements of § \_\_.20(e)(2) also be applied to sponsored funds relying on the other new proposed exclusions for credit funds, venture capital funds, and family wealth management vehicles? Why or why not?

Documentation may only benefit those big law or consulting firms. Price risk shifted to upstream banks, but banks don't necessarily have better way to manage it. Yet, it gives rise to credit and liquidity risks that can possibly become systemic risk to the overall financial system. New risk may be introduced in the process of reducing price risk. Banks should cautiously enter into hedges instead of constant flipping between buy/ sell hedges. All these have to be reviewed in-depth through improved surveillance and risk control techniques. If regulators still living in age of flipping policies and procedure documents without diving into issues about consistency, possible exploitations, and/or hidden risks under the guise of central risk book, etc., good luck trying to catch the rogues.



## D.) Limitations on Relationships with a Covered Fund

We acknowledge that creditors' rights are more advantages for priority claims in case of default than equity rights. Then we looked at the listed characteristics that the agencies are proposing to remove related senior loan or senior debt interest from definition of ownership interest:

- (1) under the terms of the interest, the holders do not have the right to receive a share of the income, gains, or profits of the covered fund, but are entitled to receive only certain interest and fees, and fixed principal payments on or before a maturity date;
- (2) the right to payments are absolute and cannot be reduced because of the losses arising from the covered fund's underlying assets; and
- (3) the holders of the interest do not have the right to receive the underlying assets of the covered fund after all other interests have been redeemed or paid in full (excluding the rights of a creditor to exercise remedies upon the occurrence of an event of default or an acceleration event).

We think the agencies did a commendable job identifying these reasonable criteria, and suggested the allowance of creditor's right to participate in the removal of an investment manager for cause or to nominate or vote on a nominated replacement manager upon an investment manager's resignation or removal during an event of default.

In fact, per our submitted comments<sup>3</sup> in 2018, it highlighted a controversy aspect about "Super 23A". On one hand, it enables banks to be more diligent to discern what is, or is not, a toxic transaction. On another hand, the inadvertent side effect – who is going to pick up these unwanted assets from bank and affiliates, given banks can no longer "internalize" troublesome transactions? Specifically, legacy collateralized loan obligations' (CLOs) problem is the 5-10% bucket that has poor quality corporate bonds mixed in with good quality loans. Given CLOs almost always sold in Rule 144A and Reg. S using §3(c)(7) ... many CLO provide rights to a "controlling class" of senior debt security holders in designation of investment managers, creating the potential to hold "ownership" interest. That being said, the workaround to address this issue is by controlling class waiver and issuance of non-voting sub-class<sup>25</sup>, and cited 248.10(c)(8) for available exemption and FAQ#4 for appropriate relief. Yet, I leaved a remark stating Volcker's limitation on relationships with a covered fund is a point for Congressional debate.

The agencies should be remind of this case – Deutsche Bank left holding ~\$380 million stake in a "theme park operator" after failing to unload shares acquired for a placement.<sup>26</sup> This is certainly not the only example of banks retaining a block of stock it had been hired to sell, but it showcased how an outsized "appetite" and inability to timely "detoxify" can destabilized the bank off its balance.<sup>27</sup>

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<sup>25</sup> <https://media2.mofo.com/documents/151106livingwithvolckerrule.pdf>

<sup>26</sup> [www.4-traders.com/ABERTIS-INFRAESTRUCTURAS-69642/news/Deutsche-Bank-left-with-7percent-of-Merlin-as-secondary-sales-struggle-19986484/](http://www.4-traders.com/ABERTIS-INFRAESTRUCTURAS-69642/news/Deutsche-Bank-left-with-7percent-of-Merlin-as-secondary-sales-struggle-19986484/)

<sup>27</sup> <https://www.nytimes.com/2016/10/03/business/dealbook/deutsche-banks-appetite-for-risk-throws-off-its-balance.html>



My point is: the matter about relationships with covered funds is in effect tied to banking entities being diligent to set their RENTD. Being prudent is absolutely important when dealing with CLOs, ABCP conduits, and the like. I can understand that given the current market turmoil amid Coronavirus situation that scooping up these troubled assets may help to restore financial stability. So, “Stress RENTD” is a way out that I long advocated for in order to offer temporary relief in crunch time. If the agencies insist to relax this part of the Rule, I have no objection provided there will be periodic review of such exposure not over certain set threshold.

**Question 71.**

What impacts would the proposed amendments to section \_\_.14 have on the safety and soundness of banking entities, and on the financial stability of the United States? Would the activities permitted under the proposed amendments to section \_\_.14(a) of the implementing regulations promote and protect safety and soundness of the banking entity and U.S. financial stability, and if so, how?

Obviously there are risks, but the agencies did a commendable job listed some reasonable criteria to preserve safety and soundness standard. That being said, we prefer to offer temporary relief via “Stress RENTD” amid the current turmoil situation, but would have no objection if the agencies decided to move forward with this part of the Rule change. Please see earlier part of this section for explanations.

**Question 72.**

Are there other services that a banking entity typically provides to sponsored funds or funds for which it acts as an investment adviser that would be prohibited under section 13(f)(1) of the BHC Act and section \_\_.14 of the implementing regulations as proposed to be amended? What would be the impact on the safety and soundness of the banking entity, and the financial stability of the United States, of permitting a banking entity to engage in such transactions with a related covered fund?

I think the proposal already broaden much, but in view of current market turmoil, covered transactions in connection with payment, clearing, and settlement services may also be helpful to restore financial stability. After all, it is better to be prudent and not further extending it to “other services” other than what already listed here.

**Question 73.**

Should the agencies amend section \_\_.14 of the implementing regulations to permit banking entities to engage in additional covered transactions in connection with payment, clearing, and settlement services? Why or why not? What would be the impacts of permitting banking entities to engage in payment, clearing, and settlement services with related covered funds on the safety and soundness of the banking entity? What would be the impacts of such an approach on U.S. financial stability?

Please see our respond to Question 72 and earlier paragraphs of this section.



**Question 74.**

Should the agencies impose any additional or different qualitative or quantitative limits on the covered transactions contemplated by the proposed amendments to section \_\_.14(a) of the implementing regulations? Why or why not? For example, should the agencies impose a quantitative limit of any kind on the covered transactions that would not be subject to the prohibition in section 13(f)(1) of the BHC Act? If the agencies were to impose a quantitative limit on such covered transactions, on what should such limits be based (e.g., based on the banking entity's tier 1 capital, the size of the fund, or some other measurement), and what limits would be appropriate?

Yes. Whatever threshold limit the agencies are going to set should be reviewed periodically based on normal versus market stress conditions. Please see earlier paragraphs in this section for explanations.

**Question 75.**

Is the proposed approach to addressing transactions that are exempt under Section 23A and payment, clearing, and settlement activities effective? Why or why not? Is there a better approach to addressing these types of transactions?

No objection, please see earlier paragraphs in this section for explanations.

**Question 76.**

The proposal would require that any payment, clearing, or settlement activity be settled within five business days. Is this length of time sufficient to effectuate the proposed permitted activities? Why or why not? Is another length of time, such as three days, more appropriate or consistent with current market practices? Should the agencies adopt a limit that adopts the shorter of five days or industry standard settlement time for a particular financial instrument?

"Shorter of five days or industry standard settlement time for a particular financial instrument" seems reasonable.

**Question 77.**

Should the agencies, for the purposes of section \_\_.14(a)(2)(iv) of the proposed amendment, impose on the purchase of assets a requirement that the banking entity comply with the requirements of 12 CFR 223.15(a), as if such banking entity and its affiliates were a member bank and the covered fund were an affiliate thereof?

12 CFR 223.15(a)'s requirement on banks that they "may not purchase a low-quality asset from an affiliate unless, pursuant to an independent credit evaluation, the member bank had committed itself to purchase the asset before the time the asset was acquired by the affiliate," make sense. The agencies should impose it in order to be in synch with the stable run-off of toxic assets' objective of the Rule.

Yet, in view of current market turmoil, the subject matter here is going to be controversial. Thus, recommend the use "Stress RENTD" to offer temporary relief in order to restore financial stability.





## **E.) Ownership Interest**

### **Question 78.**

Under the proposal, the right to participate in the removal of an investment manager for cause, or to nominate or vote on a nominated replacement manager upon an investment manager's resignation or removal, would be limited to removal or replacement upon the occurrence of an event of default or an acceleration event. Commenters noted in comments on the 2018 proposal that loan securitizations may include additional "for cause" termination events (e.g., the insolvency of the investment manager; the breach by the investment manager of certain representations or warranties; or the occurrence of a "key person" event or a change in control with respect to the investment manager) that might not constitute an event of default. Should the proposal be expanded to include the right to participate in any removal of an investment manager for cause, or to nominate or vote on a nominated replacement manager upon an investment manager's resignation or removal, whether or not an event of default or an acceleration event has occurred? Why or why not?

Being consistent with our proposition of no objection to the proposed change to limitations on Relationships with a Covered Fund, we also have no objection in here, but preferably use of "Stress RENTD" to offer temporary relief instead of a permanent Rule change. This is because the said right to participate in a removal decision can be very subjective, which makes it very hard for regulators to enforce going forward.

### **Question 79.**

Under the current rule, an interest that has the right to receive a share of the income, gains or profits of the covered fund is considered an ownership interest. Should the agencies modify this condition to clarify that only an interest which has the right to receive a share of the "net" income, gains or profits of the covered fund is an ownership interest? If so, why?

Let's be reminded of the \$6.2 billion loss in the 2012 JPMC case that taught some painful lessons<sup>24</sup>, such as: "Increased risk without notice to regulators, Mischaracterized high risk trading as hedging, Hid massive losses, Disregarded risk, Dodged regulatory oversight, Mischaracterized the portfolio, etc." "Net" reporting is one of many devastating causes in this case. The agencies should look for all details.

### **Question 80.**

Is the proposed safe harbor appropriate? Why or why not? Do the proposed conditions under the safe harbor sufficiently alleviate concerns that a senior debt instrument would not be construed as an ownership interest? If not, what amendments should be made to the proposed conditions under the safe harbor or what additional conditions should be added and why? In particular, should the reference to "fixed principal payments" under the safe harbor condition (1)(ii) be replaced with "contractually determined principal payments," "repayment of a fixed principal amount," or any other similar wording that may be more representative of typical principal distributions under various types of debt instruments, including asset-backed securities?





The emphasis is about the manner of speculative bets that may constitute as Volcker violation, not necessarily the type of the instrument or investment vehicle per se. Safe harbor requirements make sense, but the regulatory examinations should review related matters on a case-by-case basis.

### Question 81.

Should the safe harbor be limited only to senior debt instruments, as proposed? Why or why not? If so, do the proposed conditions sufficiently distinguish between senior debt instruments and other debt instruments?

Please see our respond to Question 80.

### Question 82.

Should the agencies modify the methodology of calculating a banking entity's compliance with the aggregate fund limit and covered fund deduction in the manner proposed? Why or why not? Would the proposed revisions pose any risk that a banking entity could evade the aggregate fund limit and covered fund deduction, and if so, how? Would additional restrictions on the treatment of restricted profit interests be appropriate?

Risks are going to be heightened by the agencies' proposed revision. Whatever threshold limit the agencies are going to set should be reviewed periodically based on normal versus market stress conditions. As mentioned in earlier paragraphs of the "D.) Limitations on Relationships with a Covered Fund" section, this, or the entire Volcker Rule, all boiled down to "RENTD" – reasonable securities inventory. We are hugely disappointed to see RENTD being watered down during 2019 revision<sup>5</sup>.

I can understand that given the current market turmoil amid Coronavirus situation that scooping up troubled assets may help to restore financial stability. So, "Stress RENTD" is a way out that I long advocated for in order to offer temporary relief in crunch time.

After all, how or what is the methodology of calculating a banking entity's compliance with the aggregate fund limit and covered fund deduction depends on quality of assets, liquidity, and normal versus stressed market conditions. "Reasonableness" within the following contexts would be key determination factors:

	Market	Clients	Instruments
Risk Management	CCAR (COREP/FINREP/FDSF) baseline / stress scenarios • US deep recession • Sig. decline in asset prices & increases in risk premia • Slow down in global economy • Global shock on large trading, PE & derivatives position ...	• Underwriting a/c – holding period, type of counterparty • Appendix B: how much trading risk must be hedged & how quickly - policy by unit • Appendix C: allocated risk level, leverage ratio, ops-risk events (scholastic), ...	• Risk limits: large counterparties, exposures, concentration, VaR, offsetting long/short ( <a href="#">BCBS246</a> ) • Risk Types - losses from lending collateralized by immovable property and/or illiquid assets • Delta hedge* of non-linear positions with linear instruments
Liquidity	Duration gap, portfolio immun., liquidity coverage, refinancing risk, local/int'l MM funding ...	• Stable client's / own funding • EoD repo, multi-bank cash concentration, resident a/c	Asset encumbrance, x-border cash concentration, x-currency pooling, Interest enhancement structures
Securities Inventory	• Maker-taker pricing model • Statistical arbitrage vs market making (case: Knight Capital) • Meaningful quoting, demand of liquidity timing, rebalancing • Stub quotes/agency obligation • Locked & crossed markets & 'trade-through' principle ...	• Channel strategy / appetite that max sales opp. and achieve high levels of product availability • Set up separate trading a/c: lending, syn. loan, liquidity management, underwriting, and market making	• ABC analysis (fast/slow) • Reliability of counterparty in supplying certain securities • Migration analysis: deterioration/ project losses on loans in accrual loan portfolio, changes in fair value on loans held for sale, ... • Yield, paid-off behavior, ...



## **F.) Parallel Investments**

This is the so called proprietary trading in an arm's length, but without the 3% limit! Per my submitted comments in 2017<sup>2</sup> and reiterated in 2018<sup>3</sup>, "...Many former bankers indeed join or start their own HF/PEs that, surprisingly, has a positive effect on the market with more diversified players. Though some bank alumni at HF/PEs do receive sponsorship money (up to 3%) from their old employers, suggesting implicit control by banks (at arm's length), there are rules (Super 23A/23B) guiding affiliated transactions. To curb bank alchemists<sup>28</sup> from circumventing the Rule, the covered fund definition has to be broad enough to scrutinize who might be behind the scenes involving the banking entities in high-risk proprietary trading, as well as their investment in, sponsorship of, and other connections with, entities that engage in investment activities for the benefit of banking entities, institutional investors and high-net worth individuals."

Think about it which banking entities would dare to self-disclose that their investments might not be in compliance with applicable laws and regulations, including any applicable safety and soundness standards. When, for example, 2 or 3 of these investments can cover the loss of the other 7 or 8 out of 10 different bets, in turn, this may drive management to be less stringent in their evaluation process. So, the agencies' expectation is largely meaningless, and there is no good way to catch such speculative behaviors that may potentially be considered Volcker violations or attempts to evade the restrictions of section 13. The 3% cap is at least effective to: (1) limit related exposures so losing bets may not be as detriment or disruptive to the banking entities' core financial health; (2) these arms' length investments have a higher chance of acting independently than their sponsoring banks over exerting influence over them.

That being said, I am okay if the agencies may plan to raise the cap limit from 3% to 6%, or use a "Stress RENTD" to offer temporary relief during crunch time. The purpose of this cap is to force banks making conscious decision to be "selective" and "prudent" in their parallel investments process. The agencies should discourage parallel investments that run like "Algo-wheels"<sup>29</sup> or other "wheel of fortune".

### **Question 83.**

Should the agencies adopt the proposed rule of construction in section \_\_.12(b)(5) that would address direct investments made by banking entities alongside covered funds by clarifying in the rule text that banking entities are not required to treat such direct investments alongside a covered fund as an investment in the covered fund as long as the investment is made in compliance with applicable laws and regulations? Why or why not? What, if any, modifications to the scope of the proposed rule of construction should be made? Is the proposed condition on the proposed rule of construction

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<sup>28</sup> <https://www.amazon.com/The-End-Alchemy-Banking-Economy/dp/0393247023>

<sup>29</sup> <https://www.bloomberg.com/professional/blog/whats-algo-wheel-care/>



appropriate? If not, how should the agencies modify the condition, and why? Should the agencies provide any additional guidance or requirements regarding the condition?

No, please see earlier paragraphs in this section for explanations.

#### **Question 84.**

Do commenters believe that the proposed rule of construction will provide banking entities with clarity about how a banking entity should treat its otherwise permissible investments alongside a covered fund under the implementing regulations? Why or why not? If not, what additional modifications should be made?

No, it only blurs things benefiting bank alchemists. Please see earlier paragraphs in this section for explanations.

#### **Question 85.**

Would the proposed rule of construction create any opportunities for evasion, for example, by allowing a banking entity to structure parallel investments and co-investments to evade the restrictions of section 13? Why or why not? If so, how could such concerns be addressed? Please explain.

Yes, please see earlier paragraphs in this section for explanations.

#### **Question 86.**

Do commenters agree that investments made by a director or employee alongside a covered fund should not be treated as an investment in the covered fund? Why or why not? Do commenters agree that the requirements under section \_\_.11(a)(7) that limit the directors and employees that are eligible to invest in a covered fund organized and offered by the banking entity to those who are directly engaged in providing investment advisory, commodity trading advisory, or other services to the covered fund should not apply to any such investment? Why or why not? Should the agencies provide additional rule text addressing director and employee investments alongside covered funds? Are there any additional conditions that the agencies should consider placing on director and employee investments made alongside a covered fund? Are there any modifications to the agencies' proposed treatment of director and employee investments or proposed rule of construction that commenters believe is necessary in order to accommodate director and employee investments alongside a covered fund that are made through employee securities companies or other types of employee compensation arrangements? If so, please explain what modifications would be necessary or appropriate and the rationale for such modifications.

It is not necessarily the investments "made by" a director or employee alongside a covered fund being problematic per se, but the "manner" of speculative bets that may constitute as Volcker violation.

Please see earlier paragraphs of this section for elaborated discussion.



**Question 87.**

The proposed rule of construction would not prohibit a banking entity from having investment policies, arrangements or agreements to invest alongside a covered fund in all or substantially all of the investments made by the covered fund or to fund all or any portion of the investment opportunities made available by the covered fund to other investors. Should the agencies impose any additional limitations on a banking entity's investment policies, arrangements or agreements to invest alongside a covered fund? Why or why not? If the agencies were to impose such limitations, should the agencies adopt the approach used to define "contractual obligation" in the Conformance Rule? Why or why not? Keep the 3% cap, or raise it to 6% max, but NOT excluding parallel investments from counting as part of the cap limit. Investment policies can be well articulated documents, but potentially be useless if the banking entities do not "walk the talk". Again, the "manner" in the actual investment practices is something that the regulators may want to scrutinize if there might be speculative behaviors. Please see earlier paragraphs in this section for explanations.